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RE: RIN 1901-AB21
Notice Of Proposed Rule Making, Energy Policy Act Of 2005
Title XVII Innovative Technologies Loan Guarantee Program
Comments of Agrium U.S., Inc.

AGRIUM'S INTEREST IN THE LOAN GUARANTEE PROGRAM

Agrium U.S. Inc., owns and operates the Kenai Nitrogen Operations (KNO) a manufacturing facility located in Kenai, Alaska, that relies upon natural gas as a feedstock to produce ammonia and urea fertilizers. Like many U.S. fertilizer manufacturers, we are unable to assure ourselves of a reliable, long term, reasonably priced supply of natural gas, the primary feedstock required for fertilizer production. As a result, KNO actively is evaluating the feasibility of constructing a coal gasification facility to produce the necessary hydrogen, nitrogen and carbon dioxide feedstocks for fertilizer production. As part of our feasibility evaluation, we have determined that the innovative technologies loan guarantee authority of Title XVII of the Energy Policy Act of 2005 (EPAct) could be of significant value to the project.

The KNO facility was constructed in 1968 and expanded in 1977. It is the second largest nitrogen complex in North America with the capacity to produce in excess of 2.0 million tons of fertilizer per year when operating at full capacity. KNO is one of the largest manufacturers in Alaska, employing 230 employees when operating at full capacity. It is one of Alaska's few value added industries – for every one thousand cubic feet of natural gas used, more than $9 in total economic output is generated.

Since 2002, however, KNO has been confronted with ever deepening natural gas supply shortages which have caused a reduction in operations to 50% in 2005, 2006 and 2007. Because we had only an assured supply of natural gas for six months in 2007, the plant was shut down from October 23, 2006 until May 1, 2007. If we are not successful in arranging additional supplies beyond October 31, 2007, we will be forced to permanently shut down the plant. Closing the KNO facilities will have a devastating effect on the Kenai Peninsula area of Alaska -- 230 high paying skilled jobs will be eliminated and another 420 indirect jobs will be lost along with the more than $100 million KNO injects into the Alaska economy each year. It will also add to the long list of domestic fertilizer production facilities that permanently have shut down due to feedstock pricing and supply issues.

To maintain operations at the KNO facility, Agrium must find a long-term supply of feedstock to substitute for natural gas. Fortunately, Alaska holds multi-year supplies of undeveloped coal making coal gasification a potential solution to providing the long-term feedstock that is essential to keep KNO operational.

In 2005, KNO initiated a three-year feasibility study to examine the use of gasification technology utilizing Alaskan coal and other appropriate indigenous fuel resources to produce the hydrogen, nitrogen and CO_2 we need to manufacture fertilizer. Our preliminary estimates are that the total cost of the gasification project will be between $1.5 and $2 billion.

KNO is in a substantially different position than most other U.S. industrial firms that are reliant on natural gas and that are evaluating a gasification project. These other firms basically have three options from which to choose – continue current operations using high priced natural gas for energy and feedstock; convert to coal or another alternative source of energy and feedstock by installing gasification technology; or cease U.S. operations and move overseas. Because KNO does not have an assured supply of natural gas at any price, we in effect have only two options – develop a coal gasification capability or permanently close the facility.

Our limited options do not mean, however, that we can construct the project regardless of the economics. We still must market our ammonia and urea competitively. And, as production of fertilizer shifts from traditional industrialized nations to the areas of the world with low cost stranded natural gas, these areas are setting the world price. As a consequence, KNO is exploring every opportunity to reduce the risks and costs and improve the economics of the proposed coal gasification project.

GENERAL COMMENTS

KNO has evaluated the Title XVII loan guarantee program as one of the opportunities to reduce the risks and costs. Our project envisions using gasification technology in an industrial application to provide feedstocks for the manufacture of nitrogen fertilizer products. KNO believes that this particular application of gasification technology has not been used on a commercial scale anywhere else in the United States and therefore our project clearly fits within the intent of the statutory language of Section 1703(a)(2) of EPAct which requires the project to "employ new or significantly improved technologies as compared to commercial technologies in service in the United States…".

It appears that the KNO project is precisely the type of project that the Congress intended to promote with the Title XVII loan guarantee program. Unfortunately, the policies and procedures proposed in the Department of Energy's Notice of Proposed Rulemaking (NOPR) will diminish the value of the loan guarantee program to the KNO project to the point where it is unlikely measurably to reduce costs and risks of the project.

Agrium appreciates the Department's attempt to balance the goal of the Title XVII loan guarantee program – to encourage commercial use of innovative energy-related technologies – with the desire to limit the financial exposure of the federal government. However, there is no balance in the NOPR. It appears that whenever the Department had an opportunity to strike such a balance, it tilted in favor of protecting the government from risk. This approach defeats the fundamental purpose of the loan guarantee program which is for the federal government to <u>share</u> the risk of developing energy-related technologies that are not yet commercially proven. In exchange for this risk sharing, U.S. consumers and taxpayers will benefit from the commercialization of technologies that will enhance domestic energy security and lower the emissions of greenhouse gases. The Department seems to have completely ignored the benefit side of the equation in drafting the NOPR.

Discussed below are several specific concerns that Agrium has identified in the NOPR.

1. Definition Of "General Use" For The Determining Eligible Projects

The statute does not allow loan guarantee coverage for technologies that are "in general use in the commercial marketplace." The NOPR proposes to define "general use" as either: 1) a technology that has been ordered for, installed, or used in five or more commercial projects in the U.S. at the time the loan guarantee is issued; or 2) a technology that has been in operation in a commercial project in the U.S. for 5 years. Under this proposal, if a technology merely has been ordered for five commercial projects, regardless of whether it has been installed or actually used in any project, it is considered to be in "general use." In the alternative, if a technology has been in use in a single project for five years, it is also considered to be in "general use."

This proposed definition is overly simplistic for the types of projects that are likely to apply for a loan guarantee. It does not contemplate that certain technologies may be in "general use" with respect to a particular application but may be commercially unproven in other applications. Nor does it take into account the several general characteristics, such as size, process configurations, and technology modifications that should be considered when applying the "general use" definition.

2. Guarantee Limit of 90% of Project Debt

Section 1702(c) of EPAct limits the Secretary's authority to issue a loan guarantee to ..."an amount equal to 80 percent of the project cost..." There is no limit in the statute on the percentage of the project debt that can be guaranteed provided the loan guarantee coverage does not exceed 80% of the project costs. The Federal Credit Reform Act of 1990 does not address the issue of percentage loan coverage for federal loan guarantees either. Administrative practice in other federal loan guarantee programs allows for flexibility in setting loan guarantee limits up to statutory caps.

This restriction reduces the value of the loan guarantees significantly by requiring a project to obtain non-guaranteed debt that will be very expensive, thereby compromising project economics because lower costs cannot be passed on to project off takers in the form of more competitive product prices. A principal purpose of the Title XVII loan guarantee program is to support technology that is not yet fully commercial. Higher costs reflect that pre-commercial status. The proposed level of Title XVII loan guarantee coverage directly comprises the effort to lower costs and reduce risks.

An appropriate concern of the government, and one that we share, is to insure that the government is not the only party at risk in the event of partial or total project failure. Ultimately, it is the equity investors and project developers that must take this responsibility and it is the same parties that stand to lose their investment.

3. *Pari Passu*

DOE interprets the "superior rights" provisions of EPAct Section 1702(g)(2)(B) as prohibiting *pari passu* security structures and requiring holders of non-guaranteed debt to be subordinate to any DOE claims under the loan guarantee. There is no basis for this interpretation. First, Section 1702(g)(2)(B), by its terms, only applies to DOE's rights "with respect to property acquired pursuant to a guarantee..." meaning after a default. It does not apply to DOE's rights under the financial instruments themselves. Moreover, Section 1702(d)(2), which provides that the obligation guaranteed by DOE cannot be subordinate to other financing, clearly permits pari passu financing (where senior lenders share equally and ratably in right of payment and in the security in proportion to their contribution to debt).

DOE's interpretation is also contrary to standard lending practice. The no *pari passu* provision of the NOPR will significantly limit the willingness of top-tier commercial lenders to provide loans to Title XVII eligible projects, effectively requiring more expensive sub-debt financing structures for these projects. This provision will limit the availability of financing for projects, and could have the perverse effect of attracting and rewarding less financially sound projects that have limited access to top-tier lenders and are willing to use more expensive debt financing structures.

4. Stripping of Guaranteed Debt

The NOPR prohibits the "stripping" of the guaranteed portion of the debt from the non-guaranteed portion of the debt. There is no statutory basis for this restriction, and it only further limits the attractiveness of the loan guarantee program for potential lenders and constrains the availability of financing for eligible projects.

Lenders who participate in other federal loan guarantee programs often fund their loans by transferring the loans to a special-purpose vehicle that holds only 100% federally guaranteed instruments, then sell interests in those vehicles. These vehicles are an efficient mechanism to fund and spread the risk of these loans. They are necessary because of the very thin spreads and limited profitability of federal loan guarantee programs. The prohibition on stripping will prevent lenders from using such mechanisms, thereby reducing potential lenders' willingness to participate in the program.

5. Credit Subsidy Costs

Agrium has two concerns with the manner in which the NOPR addresses credit subsidy costs. First, DOE has no authority to limit payment of such costs only to the self-pay method. Section 1702(b) unequivocally allows those costs to be paid either through an appropriation or by the borrower. The fact that DOE has not requested an appropriation for such costs cannot and should not prevent a borrower from seeking such an appropriation from the Congress for the credit subsidy costs of its project.

Second, the NOPR does not provide any indication of how DOE will calculate the subsidy cost. The calculation of this cost should be entirely transparent so that the borrower is able to accurately calculate his costs. Since the subsidy cost will be paid by the borrower, it is imperative for the borrower to be able to budget for the subsidy cost when planning a project. This is especially true if DOE does not allow the subsidy cost to be included in the calculation of project cost.

6. Receipt Of Other Forms Of Governmental Assistance

DOE states in the NOPR that it is desirable that each project receive only one form of governmental assistance. While receipt of other governmental assistance does not disqualify a project from receiving a Title XVII loan guarantee, DOE will consider the extent to which a project will receive other governmental assistance.

EPAct 2005, as well as other legislation, includes a number of different provisions to facilitate and encourage the construction of advanced coal-based facilities, such as the investment tax credits for advanced coal-based generating facilities. Participation in these programs should not limit a project's eligibility for Title XVII loan guarantees. These initiatives are intended to be complementary, not exclusive.

In the event that a project obtains other forms of governmental assistance and a loan guarantee under Title XVII, the cost of the loan guarantee should be adjusted to reflect the reduced risk of default on the underlying debt obligation as a result of the other support.

7. Credit Subsidy Costs And Administrative Fees Paid To DOE May Not Be Included Within Total Project Costs

The NOPR excludes the borrower-paid subsidy cost and administrative fees paid to DOE from the definition of project cost. These costs, in fact, are financing costs incurred and expended by the sponsors and should be included in the calculation of project cost. The exclusions are inconsistent with the treatment of similar costs in commercial project financing and in other federal financial assistance programs.

We appreciate the opportunity to comment on these proposed regulations and look forward to working with the Department in the future.

Sincerely yours,

Lisa Parker

Lisa Parker by

Thomas Cl Roberts
Counsel

cc: Senator Ted Stevens
Senator Lisa Murkowski
Representative Don Young